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C O N F I D E N T I A L SECTION 01 OF 02 ANKARA 001153

SIPDIS

STATE FOR P, E, EUR AND EB
TREASURY FOR U/S TAYLOR AND OASIA - MILLS
NSC FOR QUANRUD AND BRYZA

E.O. 12958: DECL: 02/21/2013

TAGS: [EFIN](#) [PREL](#) [EAID](#) [TU](#)

SUBJECT: A VERY WORRIED CENTRAL BANK GOVERNOR

(U) Classified by Economic Counselor Scot Marciel. Reason:
1.5(b,d).

11. (C) Summary: Central Bank Governor Sureyya Serdengeçti told us February 21 that, in his view, the government does not understand the economic consequences of failing to come to agreement on the U.S. assistance package or the IMF program. He is deeply worried that, based on their lack of economic understanding, government leaders may make "fatal" decisions. Serdengeçti insisted that any U.S. assistance must be conditioned on performance under the IMF-backed program, saying the government otherwise will use the funds to finance populist programs that will lead to "catastrophe" in a matter of months. At the same time, he warned that the GOT likely will blame any failure to reach agreement with the Fund on the U.S. (i.e., U.S. blocks the IMF review so it has an excuse not to disburse its assistance). For this reason, Serdengeçti is urging IMF officials to adopt a higher profile to differentiate the Fund from the U.S. in the public mind. End Summary.

12. (C) Central Bank Governor Sureyya Serdengeçti (strictly protect) asked to see EconCouns privately on February 21. In the meeting, Serdengeçti said he was deeply concerned about the government's efforts to de-link the U.S. assistance package from the IMF program. This effort, he said, raised grave doubts about the government's intentions on economic policy. After three months in office, the government still does not understand why it needs a stabilization/reform program and why there is no alternative. Anti-reform elements in the business community are lobbying the government to return to the old way of doing business. Since "no one in the government leadership understands," there is no one to push back. The government's failure to understand economics, he said, may lead to "fatal" decisions.

13. (C) In this regard, Serdengeçti said he was particularly worried by Minister Babacan's statements that U.S. assistance should not be linked to the IMF program. He has been trying for months to explain to Babacan and others that the best way to limit the damage from an Iraq war is to implement the IMF program. Despite his and Treasury U/S Oztrak's efforts, however, government leaders "are not aware of how fragile the situation is. They still think we can do without the IMF, and in fact want to get rid of the IMF." Normally, the floating exchange rate regime would send warning signals that might prompt the government to shift its stance. However, markets are so distorted by Iraq-related issues that they are not sending those signals.

14. (C) Serdengeçti argued that the U.S. should insist on conditioning its aid on GOT performance under the Fund program. If not, the government will use the assistance to finance populist policies, which will lead to "catastrophe" in a matter of months. At the same time, he warned, the press already is claiming that the U.S. is blocking an IMF deal as a way of enhancing its leverage. If Turkey and the U.S. reach agreement on an assistance package, but Turkey fails to reach agreement with the Fund, Turkey will almost certainly blame the U.S. for blocking the Fourth Review (as a way out of U.S. assistance commitments). For this reason, he said, it is critical that the two issues be differentiated in the public's mind. The way to do this, he suggested, is for the Fund to adopt a higher profile and to talk publicly about the importance of the reform program so that it demonstrates to the public that its decisions are independent, even if U.S. decisions are dependent. Serdengeçti plans to raise this idea with Fund officials shortly. (Comment; Minister Babacan and others in the government already are hinting that the IMF is being unusually and unreasonably tough, though they have not yet explicitly blamed that toughness on us. End Comment)

15. (C) If there is no U.S.-Turkish agreement, Serdengeçti

predicts a sharp market reaction and serious financial problems in the near future. Unfortunately, the government does not appreciate how serious the situation is, and seems to think it can manage its way through without either the U.S. assistance or the IMF program. "Their lack of awareness makes me very scared." EconCouns noted that Treasury U/S Oztrak, who understands the situation well, is still in government and presumably is alerting the government to these dangers. Serdengecti responded that Oztrak had been explaining realities for months, but "Babacan just doesn't understand." If, as the local press is reporting, the government fires Oztrak in the coming weeks, it will demonstrate that they really have no idea what they are doing.

PEARSON